14 U.S. 618 / (17)

No. 349

Office - Supreme Court, U.
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CHARLES ELMORE

IN THE

Supreme Court of the United States

OCTOBER TERM 1941.

THE DETROIT EDISON COMPANY,
Petitioner,

against

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

PETITION FOR WRIT OF CERTIORARI.

TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

AND

BRIEF IN SUPPORT THEREOF.

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August, 1941.

Pandick Press, Inc., 22 Thames St., New York, U. S. A.

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IN THE

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No. .....

THE DETROIT EDISON COMPANY,
Petitioner,

against

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

PETITION FOR WRIT OF CERTIORARI

To the United States Circuit Court of Appeals for the Sixth Circuit:

The undersigned, on behalf of the above named petitioner, pray that a writ of certiorari issue to review a final decree of the United States Circuit Court of Appeals for the Sixth Circuit rendered on May 12, 1941, in the case between the above named parties docketed therein as No. 8735.

Opinions Below.

The opinion of the Circuit Court of Appeals was handed down on May 12, 1941, and is reported in 119 Fed. (2d) 730 (R. 686). The Securities and Exchange Commission issued an opinion dated August 5, 1940, as its Holding Company Act Release No. 2208, which is reported in 7 S. E. C. 968 (R. 671).

Jurisdiction.

The decree of the Circuit Court of Appeals was entered May 12, 1941 (R. 685). This petition for a writ of certiorari is filed before August 12, 1941.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

Statute Involved.

The statute involved is the Public Utility Holding Company Act of 1935 (49 Stat. 803; 15 U. S. C. A., Sec. 79), particularly sections 1 and 2(a)(8) thereof, which are printed in the appendix, *infra*.

Matters Involved.

In the Circuit Court of Appeals the proceeding was an original one brought by petition filed pursuant to section 24(a) of the Act (49 Stat. 834; 15 U. S. C. A., Sec. 79x) to review an order of the Securities and Exchange Commission (referred to herein as the "Commission") insofar as it denied petitioner's application for an order declaring that petitioner is not a subsidiary of The North American Company (a holding company registered as such under the Act, referred to herein as "North American").

Section 2(a)(8) of the Act defines the companies which it subjects to regulation as subsidiary companies. It prescribes a formula and procedure for determining whether a company is so subject to the Act. The definition starts with a holding company ownership of 10% of voting securities, and further provides that the Commission shall declare that an applicant is not a subsidiary company of

a specified holding company if the Commission finds (i) that the applicant is not controlled by the specified holding company, and (ii) is not an intermediary of control, and (iii) that the management or policies of the applicant are not subject to a controlling influence by such holding company so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties and liabilities imposed in the Act upon subsidiary companies. Petitioner's application was made under that provision.

The Circuit Court of Appeals held that there is no evidence in the record that petitioner is controlled by North American or that it is an intermediary of control.

The petition for review was denied however, with reasoning which amounts to the theory that Congress had delegated to the Commission a discretion to determine the zone of its own jurisdiction.

The Court held in effect that the Act conferred on the Commission a double discretionary power, first, to decide what meaning should be given, as a matter of policy, to the words "controlling influence" (rather than a duty to find whether evidence satisfied the objective standard of the natural meaning of the words) and, second, to decide whether, as a matter of policy, in the public interest or for the protection of investors or consumers as conceived by the Commission, a particular subsidiary should be regulated (rather than a duty to find whether evidence satisfied the objective standards of public interest and investor or consumer protection set forth in the preceding section of the Act).

Applying that theory, the Court held in substance that the first discretion had been validly exercised by construing

"controlling influence" to mean an influence which is not controlling and is not operative, but which the Commission suspects might, if put to work, be found at some future time in relation to some future facts to exist and be partially effective; and that the second discretion had been validly exercised without any statement of fact or law on the subject by the Commission, in spite of proof (and admission by the Commission to the Court) of the absence of any harm, past or present, to the public interest or investors or consumers.

Jurisdiction was assumed by the Commission without any finding of facts or statement of opinion as to its basis. The Circuit Court of Appeals held that it was not necessary for the order of the Commission to be supported by jurisdictional findings, that the question was not raised by the petition and was incompatible with it, that it was a constitutional question and could not be raised until some order of the Commission adversely affects petitioner, and impliedly, that the order before it for review did not adversely affect petitioner.

Specification of Errors.

The Circuit Court of Appeals erred:

1. In holding that the sentence of the Act here involved delegated to the Commission discretionary powers rather than a judicial duty;

2. In its construction of the term "controlling influence" in the Act;

3. In its construction of the reference in the Act to the public interest and the protection of investors and consumers;

4. In holding that it was unnecessary for the Commission to make any specific jurisdictional findings; and

5. In denying the petition for review of the Commission's order.

Questions Presented.

The questions here to be presented are:

1. Does the sentence of the Act here involved, defining the scope of the Commission's jurisdiction, entitle an applicant to have the Commission function as a judge and jury finding objectively determinable facts, or does it require an applicant to persuade the Commission to exercise subjectively an administrative or legislative discretion?

2. What is the meaning of the term "controlling influence" in the Act?

Is it a possibly latent power, not being exercised, which might be found to be partially effective if put to a test at some future time? Or is it an influence which in fact exists and is in fact controlling at the time of hearing?

3. What are the tests for the public interest and the protection of investors and consumers, to be applied under the Act?

Must the finding required by Section 2 (a) (8) (iii) be made when there has been proven or admitted an absence of all evils enumerated in Section 1 of the Act?

4. Was it necessary for the Commission or the Court to determine whether the Commission had jurisdiction to act in this case?

Reasons for Granting the Writ.

The principle of the decision of the Circuit Court of Appeals is novel and far reaching in its implications. It involves in essence the question of whether the jurisdiction and field of control of administrative agencies is to be determined through judicial principles and processes or through the discretion of the agency whose jurisdiction is in question.

The Act defines in detail what utility holding companies and subsidiaries are subject to the jurisdiction and controls of the S.E.C. It establishes a procedure whereby such jurisdiction shall be delimited.

We are well aware of, and do not here question, the principle that, within the field of administrative jurisdiction, the administrative discretion, resting upon expert judgment, is entitled to great weight and is not lightly to be reviewed or reversed by the courts. That principle is not here in issue. Rather there is posed the question of whether an administrative agency may determine and expand its own jurisdiction through the exercise in its own favor of its own discretionary judgments.

We respectfully urge that this court should pass upon the novel question of whether the Congress intended, or the Constitution permits, a delegation of power under circumstances such that the recipient of power determines, for itself, the scope of that power through discretionary judgments, rather than through processes which are essentially judicial and dependent upon facts proven by evidence as against administrative speculation.

Construction of an Act, in terms providing for findings as a basis for regulation or exemption, so as to empower an administrative agency to act through exercise of dis-

cretion in construing the language of the law, and by basing its decisions upon speculations about the future, nullifies the obvious legislative intent to establish a judicial procedure.

It is further submitted that the Circuit Court of Appeals has overruled petitioner's objection to Federal jurisdiction in a way probably in conflict with applicable decisions of this court. It held in substance that Federal jurisdiction may be based upon consent or waiver by a litigant and that a negative order establishing a status under a Federal statute may not be reviewed to determine whether the person thereby affected is within the field of Federal jurisdiction covered by the statute.

WHEREFORE, it is respectively submitted that the petition should be granted.

JOHN FOSTER DULLES,
OSCAR C. HULL,
Attorneys for Petitioner.

August, 1941.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

For statement of the case and also statements as to the opinions below, jurisdiction, questions presented, statutes involved and specifications of errors, we refer to the foregoing petition.

POINT I

CONGRESS DID NOT DELEGATE TO THE COMMISSION A DISCRETION TO DEFINE THE SCOPE OF ITS OWN POWER. THIS PROCEEDING BEFORE THE COMMISSION WAS OF A JUDICIAL NATURE. ADMINISTRATIVE DISCRETION WAS NOT INVOLVED.

The Act provides that, upon application, the Commission "shall" declare that an applicant is not a subsidiary company of a specified holding company, if the Commission "finds" certain specified facts. Language appropriate for delegation of discretion is not used until the latter part of the section which authorizes the Commission to insert in any order granting an application, conditions requiring subsequent reports to assure the Commission that the state of facts which compels the entry of an order continues to exist so long as the order is effective.

The section is written upon the evident theory that if the facts are proven they must be found and that if the facts are found the order must be made. It defines what companies shall be within and what companies shall be without the field of Commission jurisdiction over "subsidiary companies". It is a long and carefully written statement by one thinking of matters susceptible of being

proven or disproven by evidence. No such detail or precision would be required for a grant of the broad discretions of construction and decision, exercised and so far allowed in this case.

Elsewhere in the statute (*e.g.* Sections 10-15) there often occurs a provision for ". . . such rules and regulations or orders . . . as the Commission deems necessary or appropriate . . ." The distinction so drawn between Section 2 and other sections, and between the obligation to make an order under Section 2 and the discretion to insert conditions in such an order, emphasizes the plain meaning of the words in the sentence here involved. If Congress had meant that the Commission may in its discretion exempt or regulate companies falling within the definition of subdivision (A) of the Section it would have said so, and would not have used the word "shall" in the sentence providing for exemption, nor have stated at such length the facts which an applicant for exemption must prove.

The thoroughness with which the Act described the character of interrelationships to be disproven by an applicant for exemption, is at variance with the opinion that Congress wished the Commission to formulate the rule as well as to find the facts. It also does violence to the principle that an agent cannot determine the scope of his own power by exercising a discretion not subject to judicial review.

We submit that in the absence of an explicit direction by Congress, no act should be construed as leaving its interpretation and the field of its application to be bounded only by the limits of an administrative discretion; and that a legislature may not validly delegate to an administrative body the power to establish the extent of its own authority.

POINT II

ORDINARY MEANING AND EFFECT MUST BE GIVEN TO ALL THE LANGUAGE IN A STATUTE. THIS IS TRUE HERE OF THE REFERENCE TO "CONTROLLING INFLUENCE". ITS PLAIN MEANING IS AN INFLUENCE WHICH IN FACT EXISTS AND IS IN FACT CONTROLLING.

There is no statutory definition of the phrase "controlling influence" or of either of those words. There is nothing obscure about them, nor do they interrelate with anything else in the Act. They must, therefore, be given their ordinary meaning.

The concept of a controlling influence is not mysterious. It is the same concept as that commonly expressed by the courts when they speak of the controlling part of a statute, or of a controlling decision on a proposition of law, or of controlling evidence which determines the action of a court or jury on matters of fact. Something which is controlling is a thing which must be acted upon and must be obeyed. A controlling influence is such that it compels its desired result. Anything short of that may be substantial influence or material influence, or some other kind or degree of influence, but it cannot be said to be controlling influence.

The legislative history of the Act shows that as originally introduced in both the House (H. R. 5423) and the Senate (S. 1275) the corresponding clause then used the phrase "material influence" and that this was later changed by amendment and the phrase "controlling influence" used in the final bill as enacted.

Congress deliberately took out the adjective "material" and inserted in lieu thereof the adjective "controlling". Congress thus showed that it intended that in order to

subject a company to the Act under clause (iii), there must exist something more than influence and more than a material influence—the influence must be controlling.

The Court below, however, held that the phrase "controlling influence" as used in the Act does not necessarily mean that those exercising it must be able to carry their point, that a controlling influence may be effective without accomplishing its purpose fully and that such an influence may be inferred as a "latent power" in spite of conclusive proof that no such influence is being exercised. It is submitted that such interpretation in effect repeals the word "controlling" in the Act and by judicial fiat seeks to substitute the concept of "material" which the Congress itself first considered and finally rejected.

It is further submitted that neither the opinion of the court below, nor the findings of the Commission, justifies the conclusion that petitioner has failed to prove that it is not subject to any holding company influence which under any proper construction could be regarded as "controlling".

POINT III

SUCCESSIVE CLAUSES IN THE SAME STATUTE MUST BE CONSTRUED TO BE DESIGNED FOR DIFFERENT PURPOSES. THE CONSTRUCTION BELOW RENDERS SUPERFLUOUS THE SUBSEQUENT REFERENCE IN THE ACT TO THE "PUBLIC INTEREST" AND THE "PROTECTION OF INVESTORS OR CONSUMERS".

The reference to the public interest and protection of investors and consumers is written in the Act as a qualification of the condition of being subject to a controlling influence by a holding company. Even if an applicant were subject to a controlling influence of a holding company (under any construction of the phrase "controlling influence") it

would still be entitled as a matter of substantive right to an order exempting it from regulation if it made a satisfactory showing that the character of that influence is not adverse to the public interest or to investors or consumers.

Unless the language is construed as intended to be applied in each case as a test of the character of the influence of the specified holding company upon the management and policies of the particular applicant, it would be superfluous. Moreover, unless the character of an influence is to be tested by proof of the results, or lack of results, of such influence, it would be impossible for any applicant ever to make a case which would entitle it to an order granting its application. It would always be possible for the Commission to speculate about the future (as was done in the opinion of the court below) and to say that normal corporate characteristics make it necessary or appropriate that the operating company be subjected to regulation. Such conclusion could be drawn in every case from the mere existence of a controlling influence—and has here been based upon a speculation that there may be a latent influence which might be partially effective.

The Commission gave no hint of any facts or theory upon which it based its conclusion that it did not think that petitioner had proven this phase of its case. It only said (R. 681) that "* * * In view of all the circumstances, we do not think Edison has demonstrated that it is not necessary and appropriate * * * (etc.)."

Conclusions expressed merely in the language of a statute are not sufficient to support an order. Compare *Pacific Power & Light Co.* v. *F. P. C.*, 98 F. (2d) 835 (1938); *Saginaw Broadcasting Co.* v. *F. C. C.*, 96 F. (2d) 554, 560 (1938) cert. den. 305 U. S. 613; *Tri-State Broadcasting Co.* v. *F. C. C.*, 96 F. (2d) 564, 566 (1938); *Atchison, Topeka & Santa Fe Ry. Co.* v. *U. S.*, 295 U. S. 193, 201 (1935).

In its reply brief to the court below the Commission acknowledged that there was not anything in the record from which one might imagine that any influence of North American over petitioner was harmful in any way. It made the bald claim that the Commission was entitled to regulate all relations subject to a controlling influence no matter how "good" any influence might have been proven to have been. That is a claim of discretion so unlimited, and a disclosure that its exercise will be so inflexible, that it wholly thwarts the effort of Congress to enact a rule of law for such cases. It repeals the whole reference to the public interest and the protection of investors and consumers and leaves condition (iii) of the Act with the meaning it would have had if that reference had not been included. Successive clauses in a statute must, instead, be construed so that full effect will be given to the meaning of each one. *People* v. *Luhrs,* 195 N. Y. 377, 381 (1909); *Ginsberg & Sons* v. *Popkin,* 285 U. S. 204, 208 (1932).

The result of the opinion below is to leave the Commission free to regulate any public utility company in which any holding company has any stock interest, regardless of any proof of the independence of the subsidiary or the character of the influence or the lack of harm therefrom to anyone.

The Commission hesitated, for some time, to take the extreme position we outline. In this case it waited for its reply brief and final argument in the court below. In other cases it had purported, in some degree, to give effect to the Congressional intention. See *In the Matter of West Penn Railways Company,* H. C. A. Release 953 (1938); *In the Matter of H. M. Byllesby & Co.,* H. C. A. Release 1882, 6 S. E. C. 639 (1940); *In the Matter of Wisconsin Valley Improvement Co.,* H. C. A. Release 2359 (1940).

There is no question in this case of the completeness and conclusiveness of the proof on this issue. Every evil so carefully specified in Section 1 of the Act as attendant upon the character of controlling influence which Congress intended to have regulated, was negatived by proof at the trial—as the Commission finally bore witness to the court.

Congress did not delegate to the Commission the discretion of determining what sort of influence would require regulation. It did not even leave the construction of those terms to implication from the general spirit and purpose of the law. It enumerated explicitly in Section 1 of the Act the kind of abuses which it declared to be injurious to investors, consumers and the general public, and categorically laid down the rule that "* * * it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted, to meet the problems and eliminate the evils as enumerated in this section * * *".

Petitioner submits that it is vital to public confidence in the judicial process, that the application of the rule so positively expressed by Congress, and of the elementary principles of statutory construction, be reviewed by this court.

POINT IV

FEDERAL JURISDICTION CANNOT BE CREATED BY WAIVER OR CONSENT. IT MUST EXIST. THE QUESTION MAY BE RAISED AT ANY STAGE OF ANY PROCEEDING.

Jurisdiction is the threshold of every court and commission, over which one may not cross, or drag another, without the proper credentials.

Federal jurisdiction is peculiarly limited by the Constitution but is not on that account made irrelevant to any

type or stage of proceeding. It is familiar practice for a court, of its own motion, to raise the question of jurisdiction, and for an appellate court to dismiss a proceeding when the record does not contain adequate proof of jurisdiction. *Chicago, Burlington and Quincy Railway Company* v. *Willard,* 220 U. S. 413 (1911).

In this case the Commission did not find a basis for jurisdiction or express any opinion about it. It ignored petitioner's proofs and protests on the subject. Before the Court it claimed that the question had been waived, and furthermore that it was a constitutional one and therefore could not be raised until some later attempt to enforce against petitioner other provisions of the Act. The court below, in effect, sustained those arguments.

This result treats a constitutional limitation on administrative jurisdiction differently from other limitations and thus extends the boundaries of federal power in a novel and dangerous way. The judicial and executive branches of the government do not imperil its citizens as would the new hybrid administrative bodies acting behind such a shield.

In holding that the question is prematurely raised the opinion below resurrects the negative order doctrine in a new disguise and fails to appreciate the nature and effect of the order in question. Section 2(a)(8) of the Act serves no purpose independent of other features of the Act as the Commission seems to contend. Its sole function is to define those companies which are subject to the Act as subsidiaries. The restrictions of the Act and of Rules and Regulations of the Commission are *automatically* applicable upon a determination of status under Section 2(a)(8) and a company's rights are thereby subjected not only to threats but to injury from the many restrictions and prohibitions which are directly and immediately consequent upon such determination of status.

Petitioner submits that this Court should review the action of the court below to clarify the principles governing, and to correct the practice of, lower tribunals with respect to the assertion and exercise of federal administrative power and the review of that ever increasingly important class of quasi-judicial determinations which subject the affected persons to a great body of prohibitions, restrictions and obligations without further act or order and without any judicial determination that they are properly within the scope of the asserted power.

Respectfully submitted,

JOHN FOSTER DULLES,
OSCAR C. HULL,
Attorneys for Petitioner.

Appendix.

AN ACT

To provide for control and regulation of public-utility holding companies, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Public Utility Act of 1935". (15 U. S. C. A. Sec. 79.)

TITLE I—CONTROL OF PUBLIC-UTILITY HOLDING COMPANIES.

NECESSITY FOR CONTROL OF HOLDING COMPANIES.

SECTION 1. (a) Public-utility holding companies and their subsidiary companies are affected with a national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States; (2) their service, sales, construction, and other contracts and arrangements are often made and performed by means of the mails and instrumentalities of interstate commerce; (3) their subsidiary public-utility companies often sell and transport gas and electric energy by the use of means and instrumentalities of interstate commerce; (4) their practices in respect of and control over subsidiary companies often materially affect the interstate commerce in which those companies engage; (5) their activities extending over many States are not susceptible of effective control by any State and make difficult, if not impossible, effective State regulation of public-utility companies.

(b) Upon the basis of facts disclosed by the reports of the Federal Trade Commission made pursuant to S. Res. 83 (Seventieth Congress, first session), the reports of the Committee on Interstate and Foreign Commerce, House of

Representatives, made pursuant to H. Res. 59 (Seventy-second Congress, first session) and H. J. Res. 572 (Seventy-second Congress, second session) and otherwise disclosed and ascertained, it is hereby declared that the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers of electric energy and natural and manufactured gas, are or may be adversely affected—

(1) when such investors cannot obtain the information necessary to appraise the financial position or earning power of the issuers, because of the absence of uniform standard accounts; when such securities are issued without the approval or consent of the States having jurisdiction over subsidiary public-utility companies; when such securities are issued upon the basis of fictitious or unsound asset values having no fair relation to the sums invested in or the earning capacity of the properties and upon the basis of paper profits from intercompany transactions, or in anticipation of excessive revenues from subsidiary public-utility companies; when such securities are issued by a subsidiary public-utility company under circumstances which subject such company to the burden of supporting an overcapitalized structure and tend to prevent voluntary rate reductions;

(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and materials, or enter into transactions in which evils result from an absence of arm's-length bargaining or from restraint of free and independent competition; when service, management, construction, and other contracts involve the allocation of charges among subsidiary public-utility companies in different States so as to present problems of regulation which cannot be dealt with effectively by the States;

(3) when control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as to complicate and obstruct State regulation of such companies, or when control of such companies is exerted through disproportionately small investment;

(4) when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties; or

(5) when in any other respect there is lack of economy of management and operation of public-utility companies or lack of efficiency and adequacy of service rendered by such companies, or lack of effective public regulation, or lack of economies in the raising of capital.

(c) When abuses of the character above enumerated become persistent and wide-spread the holding company becomes an agency which, unless regulated, is injurious to investors, consumers, and the general public; and it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted, to meet the problems and eliminate the evils as enumerated in this section, connected with public-utility holding companies which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce; and for the purpose of effectuating such policy to compel the simplification of public-utility holding-company systems and the elimination therefrom of properties detrimental to the proper functioning of such systems, and to provide as soon as practicable for the elimination of public-utility holding companies except as otherwise expressly provided in this title.

DEFINITIONS.

SEC. 2. (a) When used in this title, unless the context otherwise requires—

* * * * * *

(8) "Subsidiary company" of a specified holding company means—

(A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company (or by a company that is a subsidiary company of such holding company by virtue of this clause or clause (B)), unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; and

(B) any person the management or policies of which the Commission, after notice and opportunity for hearing, determines to be subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that such person be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies.

The Commission, upon application, shall by order declare that a company is not a subsidiary company of a specified holding company under clause (A) if the Commission finds that (i) the applicant is not controlled, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) either through one or more intermediary persons or by any means or device whatsoever,

(ii) the applicant is not an intermediary company through which such control of another company is exercised, and (iii) the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies. The filing of an application hereunder in good faith shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a subsidiary company of such specified holding company until the Commission has acted upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application. As a condition to the entry of, and as a part of, any order granting such application, the Commission may require the applicant to apply periodically for a renewal of such order and to file such periodic or special reports regarding the affiliations or intercorporate relationships of the applicant as the Commission may find necessary or appropriate to enable it to determine whether in the case of the applicant the conditions specified in clauses (i), (ii), and (iii) are satisfied during the period for which such order is effective. The Commission, upon its own motion or upon application, shall revoke the order declaring such company not to be a subsidiary company whenever in its judgment any condition specified in clause (i), (ii), or (iii) is not satisfied in the case of such company, or modify the terms of such order whenever in its judgment such modification is necessary to ensure that in the case of such company the conditions specified in clauses (i), (ii), and (iii) are satified during the period for which such order

is effective. Any action of the Commission under the preceding sentence shall be by order. Any application under this paragraph may be made by the holding company or the company in respect of which the order is to be entered, but as used in this paragraph the term "applicant" means only the company in respect of which the order is to be entered.

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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 349

THE DETROIT EDISON COMPANY, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Commission (R. 671)[1] is reported in 7 S. E. C. 968. The opinion of the Circuit Court of Appeals (R. 686) is reported in 119 F. (2d) 730.

[1] The original record in this case was voluminous. Counsel accordingly stipulated in the court below as to the portions to be printed. The printed record in this Court consists of the volume printed below (to which have been added the proceedings below), plus another supplemental volume filed by petitioner. All record references herein, however, relate to the original volume.

JURISDICTION

The decree of the Circuit Court of Appeals was entered May 12, 1941 (R. 685). The petition for a writ of certiorari was filed August 6, 1941. The jurisdiction of this Court is invoked by petitioner under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The petitioner, more than 10 per cent of whose voting securities are owned or controlled by a holding company (North American Company), applied to the Securities and Exchange Commission for an order declaring that it is not a "subsidiary company" under Section 2 (a) (8) of the Public Utility Holding Company Act of 1935. The basic question presented is whether the management or policies of petitioner are "subject to a controlling influence" by North American within the meaning of those provisions.

STATUTE INVOLVED

The applicable provisions of the Public Utility Holding Company Act of 1935 are set forth in the Appendix, *infra*, pp. 15–22.

STATEMENT

The petitioner, Detroit Edison Company, is an operating electric utility company. The North American Company, a holding company, owns or controls 19.28% of petitioner's voting securities.

In addition, 20.27% of petitioner's voting securities are owned by American Light & Traction Company, a subsidiary of the United Light and Railways Company, which in turn is a subsidiary of The United Light and Power Company (R. 671–672).

Petitioner is thus a "subsidiary company" in both the North American and United holding-company systems under Section 2 (a) (8) (A) of the Public Utility Holding Company Act, since more than 10% of its voting securities are owned by each of them. It brought this proceeding under the last paragraph of Section 2 (a) (8), asking the Securities and Exchange Commission to declare that it is not a subsidiary company in either system. The Commission ruled that petitioner is not a subsidiary in the United system but that it had failed to qualify for exemption with respect to the North American system since it had not shown that its management or policies "are not subject to a controlling influence" by North American within the meaning of those provisions. The findings of the Commission (R. 671–681), as approved by the Circuit Court of Appeals (R. 686–703), may be summarized as follows:

The petitioner, hereinafter referred to as Edison, was organized by North American in 1903. Its organization meeting was held at North American's offices and its first officers and directors were designated by North American. The details

of incorporation and organization were handled by the law firm of Sullivan & Cromwell, who were then, and are now, general counsel for the North American system, and since then have been counsel for Edison. Of the securities received by a syndicate, including North American, in return for the assets which were transferred to Edison, North American retained 14.73%. Its holdings of voting securities thereafter fluctuated from a low of 6.45% in 1924 to a high of 23.52% in 1931 (R. 674).

Edison's first president was also president of North American (R. 675). The first board of directors included the president of both, two other directors and members of the executive committee of North American, and a North American vice president. It also included a member of the firm of Sullivan & Cromwell; Dow, the manager of Edison; the president of General Electric Company, who became a director of North American in 1905; and two Detroit businessmen. The predominant influence of North American on Edison's board of directors has persisted since that time, and today at least four members of the present board are either associated with North American or derive their connection with Edison from North American (R. 675–678).

The personal stockholdings of Edison's officers and directors are negligible. No Edison stockholder, other than North American, appears ever

to have designated any of Edison's officers or directors, and no Edison officer or director appears to have had any relationship to any substantial Edison stockholder other than North American. (R. 677.) The continuity of the directors and the officers of Edison has been preserved through the use of the corporate proxy system. As the court below noted (R. 696):

> It is, and has been, the practice of the company to organize a proxy committee each year named by its directors, under the form of which the committees have always been instructed to vote for retiring directors if they were available. Between 1903 and 1910, an average of 80% of stockholders' votes cast at meetings were by proxy and since that time the percentage has varied from 90% to 100%.

This proxy machinery was effective to defeat United's attempt to procure representation on Edison's board of directors. Between 1925 and 1931 the United group, another public utility holding company system, acquired a large block of Edison's stock. Although North American's holdings of Edison's voting stock had fallen to a low of 6.54 per cent in 1924, it went into the market and kept close pace with United's purchases. In 1926, 1932, and 1934 United requested representation on Edison's board as a substantial stockholder, but the request was denied. In 1935, United tried unsuccessfully to force representa-

tion by attempting to break a quorum at the stockholders' meeting. It is still without representation on Edison's board (R. 679–680).

For years Edison participated with North American and its acknowledged subsidiaries in joint purchasing contracts. The arrangement was terminated in 1929, only when Edison's own purchasing power entitled it to terms commensurate with those obtainable under the joint contracts. For many years it was the only company, in addition to other statutory subsidiaries, which sent representation to North American's Station Advisory Committee, an engineers' group which compared operating methods.

North American served as Edison's fiscal agent until 1935. Until then, Edison's office, at which stock ledgers and other books were kept, was maintained in the offices of North American in New York. But thereafter, as stated by the circuit court of appeals (R. 695):

> For the sole purpose of avoiding the application of the Public Utility Holding Act, petitioner, in November, 1935 discontinued the use of the North American Company's offices and established its own on a different floor in the same building and put in charge thereof a former employee of the North American, who thereafter discontinued his connection with it. All officers of petitioner who were also officers of the North American Company at that time, resigned and petitioner's stock ledgers, its

> printed proxies and annual reports to stockholders were removed from the North American offices to petitioner's new offices and thereafter no mail was either sent or received for petitioner through the North American offices.[2] * * *

Against this background, the Commission determined that Edison had not sustained its burden of proving that it is not a subsidiary of The North American Company.

ARGUMENT

The narrow issue involved is whether Edison bore the burden of showing before the Securities and Exchange Commission that it is not a subsidiary of North American. The decision of the court below that it had not borne that burden is correct and does not call for further review.

1. Since 19.28 percent of Edison's voting securities are owned by North American, Edison is a "subsidiary company" of North American under Section 2 (a) (8) (A) of the Public Utility

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[2] These changes were all suggested to Edison by North American. In 1935 two Detroit officials of Edison went to New York and conferred with Sullivan & Cromwell and North American relative to changes necessary as the result of the passage of the Act. They wrote to Mr. Dow, president of Edison, as follows (Com. Ex. No. 34):

> Mr. Piske [North American's secretary] and Mr. Crispell [Sullivan & Cromwell partner] stressed the point that these changes will be of particular benefit to the Detroit Edison Company in eliminating any appearance of control by North American Company, and that it is desirable to have the Detroit office and officers handle as much as possible of the work now handled in New York.

Holding Company Act. But under those provisions the Commission is required upon application to declare that a company is not a subsidiary if it finds certain facts, one of which is that—

> (iii) the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies. * * *

In this case the Commission refused to find that Edison's management or policies are not "subject to a controlling influence, directly or indirectly," by North American. The record shows that there was substantial evidence supporting the Commission's action, and the court below therefore properly declined to upset its ruling.[3] As this Court remarked with respect to a cognate issue in

[3] The Government argued below and intends to renew the contention in this Court if certiorari be granted that the order of the Commission can be sustained on the alternative ground that petitioner failed also to show that it is not "controlled" by North American in the manner specified in condition (i) of section 2 (a) (8).

Rochester Tel. Corp. v. *United States,* 307 U. S. 125, 145:

> Investing the Commission [Federal Communications] with the duty of ascertaining "control" of one company by another, Congress did not imply artifical tests of control. This is an issue of fact to be determined by the special circumstances of each case.

The record shows that Edison was organized by North American; that its board of directors was entirely designated by North American; that the presence of North American representatives on its board of directors has continued throughout the years; that by reason of the management's control of proxies no other stockholder has been able to designate members of the board. The record also shows close collaboration between Edison and North American in the past in a variety of ways. Although many of the formal indicia of collaboration (such as occupancy of same office space, etc.) were eliminated in 1935 in an apparent attempt to avoid regulation, the record does not disclose any significant change in the essential relationship between the companies. Indeed, the elimination of some of the formal indicia, at the suggestion of North American and its counsel, emphasizes rather than detracts from the persistence of the basic relationship.

In these circumstances, the Commission was entirely justified in refusing to grant exemption to petitioner, and its determination in turn was properly left undisturbed by the court below. "So long as there is warrant in the record for the judgment of the expert body it must stand." *Rochester Tel. Corp.* v. *United States,* 307 U. S. 125, 145–146.

2. The fact that the relationship between petitioner and North American gives the latter a potential controlling influence over petitioner is sufficient. Petitioner's suggestion that the statute requires actual domination of its affairs by the holding company is without merit. The ever present threat of domination, i. e., the power to control, is what the statute was obviously concerned with. Compare *Rochester Tel. Corp.* v. *United States,* 307 U. S. 125, 145 where the Court approved a finding of control by the Federal Communications Comission under circumstances where one company merely had the "power to control" the functions of another, rather than actual domination of its affairs.

Similarly, it is not necessary, as contended by petitioner, that the relations between petitioner and North American are presently leading to or have led to evil results. The actual existence or non-existence of any of the evils detailed in Section 1 (b), Appendix, *infra,* pp. 15–16, is not material. Section 1 (b) declares that the national

public interest, as well as the interests of investors or consumers—

are or *may be* adversely affected—

* * * * *

(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and materials, or enter into transactions in which evils result from an absence of arm's length bargaining or from restraint of free and independent competition; * * * [Italics supplied.]

Congress thus enumerates certain situations which it considers *potentially* harmful to the public interest, and in order to protect the public interest later in the Act prohibits service, sales, and construction contracts between holding companies and their subsidiaries.[4] No attempt is made in the Act to confine the operation of its regulatory provisions to holding company systems concerning which "evil" had been discovered by the investigations referred to in Section 1 (b). On the contrary, the primary purpose of the statute is not to punish abuse, but to prevent its occurrence. To that end, innocent as well as harmful transactions are necessarily included in the enumeration of Section 1 (b) (2) above, if by their nature they are susceptible of results inimical to the public interest. It must therefore be clear that in referring in Section 2 (a) (8) to a "controlling influence * * * so as to make it necessary *or* ap-

[4] Section 13 (a), Appendix, *infra*, pp. 20–21.

propriate in the public interest * * * that the applicant be subject to the obligations * * *" [italics supplied] of the Act, Congress was simply adverting to the potential evils previously outlined in Section 1 (b).

3. Petitioner contends that the Commission has not made "jurisdictional" findings which would justify the exercise of the commerce power over its activities. But even if such findings were necessary, petitioner's position would not be advanced, for petitioner itself has initiated these proceedings, asking for an exemption from the otherwise applicable provisions of Section 2 (a) (8) (A); and if these proceedings are a nullity, petitioner is left just where it started, namely, without its desired exemption.

Moreover, no such "jurisdictional" findings are necessary. The Act does not require each subsidiary to be engaged in interstate commerce. The commerce clause comes into play only at the points where the activities of the companies are regulated, and petitioner may not here, any more than was done in *Electric Bond and Share Co.* v. *Securities and Exchange Commission,* 303 U. S. 419, 443, challenge the application of the statute *in limine* with respect to all its activities under the cloak of a proceeding to establish that it is not a subsidiary.

4. Finally, there is no substance to petitioner's contention that the decision below grants the Com-

mission a delegation of power to determine for itself the scope of its own jurisdiction. The court below did not hold that the Commission had power to determine arbitrarily what constituted "controlling influence." On the contrary, the court said only that since controlling influence may be exerted in varied and subtle ways, Congress could not promulgate a code so specific as to adapt itself to all possible contingencies and evils; and although seven types of control were recognized at the time of the passage of the Act, Congress refrained from laying down rules of thumb for the determination of controlling influence in recognition of the fact that other forms of control "may develop from the urge of individuals to avoid public regulation" (R. 699).

That the court did not hold that the Commission has discretionary power to determine the meaning of the phrase "controlling influence" is confirmed by the fact that the court itself defined the meaning of the phrase, as follows (R. 699):

> This phrase should be construed in the light of the purpose of the Act of which it is a part, and when understood in this setting and in the light of its ordinary signification, it means the act or process, or power of producing an affect which may be without apparent force or direct authority and is effective in checking or directing action, or exercising restraint or preventing free action. The phrase as here used

does not necessarily mean that those exercising controlling influence must be able to carry their point. A controlling influence may be affective without accomplishing its purpose fully.

CONCLUSION

The decision below is correct. It turns largely upon the facts and presents no question worthy of further review. The petition should be denied.

Respectfully submitted.

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APPENDIX

PUBLIC UTILITY HOLDING COMPANY ACT OF 1935, 49 STAT. 803, 15 U. S. C., SUPP. V, § 79

NECESSITY FOR CONTROL OF HOLDING COMPANIES

SECTION 1. (a) Public-utility holding companies and their subsidiary companies are affected with a national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States; (2) their service, sales, construction, and other contracts and arrangements are often made and performed by means of the mails and instrumentalities of interstate commerce; (3) their subsidiary public-utility companies often sell and transport gas and electric energy by the use of means and instrumentalities of interstate commerce; (4) their practices in respect of and control over subsidiary companies often materially affect the interstate commerce in which those companies engage; (5) their activities extending over many States are not susceptible of effective control by any State and make difficult, if not impossible, effective State regulation of public-utility companies.

(b) Upon the basis of facts disclosed by the reports of the Federal Trade Commission made pur-

suant to S. Res. 83 (Seventieth Congress, first session), the reports of the Committee on Interstate and Foreign Commerce, House of Representatives, made pursuant to H. Res. 59 (Seventy-second Congress, first session) and H. J. Res. 572 (Seventy-second Congress, second session) and otherwise disclosed and ascertained, it is hereby declared that the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers of electric energy and natural and manufactured gas, are or may be adversely affected—

(1) when such investors cannot obtain the information necessary to appraise the financial position or earning power of the issuers, because of the absence of uniform standard accounts; when such securities are issued without the approval or consent of the States having jurisdiction over subsidiary public-utility companies; when such securities are issued upon the basis of fictitious or unsound asset values having no fair relation to the sums invested in or the earning capacity of the properties and upon the basis of paper profits from intercompany transactions, or in anticipation of excessive revenues from subsidiary public-utility companies; when such securities are issued by a subsidiary public-utility company under circumstances which subject such company to the burden of supporting an overcapitalized structure and tend to prevent voluntary rate reductions;

(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and

materials, or enter into transactions in which evils result from an absence of arm's-length bargaining or from restraint of free and independent competition; when service, management, construction, and other contracts involve the allocation of charges among subsidiary public-utility companies in different States so as to present problems of regulation which cannot be dealt with effectively by the States;

(3) when control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as to complicate and obstruct State regulation of such companies, or when control of such companies is exerted through disproportionately small investment;

(1) when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties; or

(5) when in any other respect there is lack of economy of management and operation of public-utility companies or lack of efficiency and adequacy of service rendered by such companies, or lack of effective public regulation, or lack of economies in the raising of capital.

(c) When abuses of the character above enumerated become persistent and widespread the holding company becomes an agency which, unless regulated, is injurious to investors, consumers, and the general public; and it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted, to meet the problems and eliminate the evils as

enumerated in this section, connected with public-utility holding companies which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce; and for the purpose of effectuating such policy to compel the simplification of public-utility holding-company systems and the elimination therefrom of properties detrimental to the proper functioning of such systems, and to provide as soon as practicable for the elimination of public-utility holding companies except as otherwise expressly provided in this title.

DEFINITIONS

SEC. 2. (a) When used in this title, unless the context otherwise requires—

* * * * *

(8) "Subsidiary company" of a specified holding company means—

(A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company (or by a company that is a subsidiary company of such holding company by virtue of this clause or clause (B)), unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; and

(B) any person the management or policies of which the Commission, after notice and opportunity for hearing, determines to be subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more

other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that such person be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies.

The Commission, upon application, shall by order declare that a company is not a subsidiary company of a specified holding company under clause (A) if the Commission finds that (i) the applicant is not controlled, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) either through one or more intermediary persons or by any means or device whatsoever, (ii) the applicant is not an intermediary company through which such control of another company is exercised, and (iii) the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies. The filing of an application hereunder in good faith shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a subsidiary company of such specified holding company until the Commission has acted

upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application. As a condition to the entry of, and as a part of, any order granting such application, the Commission may require the applicant to apply periodically for a renewal of such order and to file such periodic or special reports regarding the affiliations or intercorporate relationships of the applicant as the Commission may find necessary or appropriate to enable it to determine whether in the case of the applicant the conditions specified in clauses (i), (ii), and (iii) are satisfied during the period for which such order is effective. The Commission, upon its own motion or upon application, shall revoke the order declaring such company not to be a subsidiary company whenever in its judgment any condition specified in clause (i), (ii), or (iii) is not satisfied in the case of such company, or modify the terms of such order whenever in its judgment such modification is necessary to ensure that in the case of such company the conditions specified in clauses (i), (ii), and (iii) are satisfied during the period for which such order is effective. Any action of the Commission under the preceding sentence shall be by order. Any application under this paragraph may be made by the holding company or the company in respect of which the order is to be entered, but as used in this paragraph the term "applicant" means only the company in respect of which the order is to be entered.

* * * * *

SERVICE, SALES, AND CONSTRUCTION CONTRACTS

SEC. 13. (a) After April 1, 1936, it shall be unlawful for any registered holding company, by use of the mails or any means or instrumentality of interstate commerce, or otherwise, to enter into or take any step in the performance of any service, sales, or construction contract by which such company undertakes to perform services or construction work for, or sell goods to, any associate company thereof which is a public-utility or mutual service company. This provision shall not apply to such transactions, involving special or unusual circumstances or not in the ordinary course of business, as the Commission by rules and regulations or order may conditionally or unconditionally exempt as being necessary or appropriate in the public interest or for the protection of investors or consumers.

* * * * *

COURT REVIEW OF ORDERS

SEC. 24. (a) Any person or party aggrieved by an order issued by the Commission under this title may obtain a review of such order in the circuit court of appeals of the United States within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith served upon any mem-

ber of the Commission, or upon any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall certify and file in the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any

such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

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U. S. GOVERNMENT PRINTING OFFICE : 1941